

EXPECTING PEAK PERFORMANCE: REQUIRING CITY AND COUNTY EFFICIENCY AUDITS



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Expecting Peak Performance: Requiring City and County Efficiency Audits

James Quintero and Parker Stathatos

Executive Summary

An independent efficiency audit investigates a governmental entity's operations and fiscal administration and identifies opportunities to eliminate waste, fraud, and abuse. According to the U.S. Government Accountability Office (2021), "Government auditing is essential in providing accountability to legislators, oversight bodies, those charged with governance, and the public" (p. 4). Ordinarily, the value of this tool is obvious; however, it holds added importance today given Texas' fiscal landscape and the threat of long-term engorgement brought about by the deluge of federal aid.

For example, the Coronavirus Aid, Relief, and Economic Security Act and the American Rescue Plan Act of 2021 provided billions of dollars to state and local governments nationwide, including nearly \$6.4 billion to Texas' largest cities and counties. As a result of this infusion, there is a significant risk that the programs and services funded through these one-time monies will become recurring budgetary features. This will put upward pressure on revenue generation and the imposition of new taxes.

Separate and apart from the deluge of federal aid, local governments in general have generated substantial income from their various revenue streams, well above the basic requirement. Consider one recent study (Quintero & Jones, 2022, p. 3): "From 2016 to 2020, property taxes generally outstripped population and inflation in most of Texas' populous cities, counties, and school districts." Due to this aggressive posture, family finances and business budgets alike have been placed under great strain. What's more, the over-collection has also fueled the growth of local bureaucracies and created an environment of excess as the constant stream of new tax money has put off hard decisions.

Thus, city and county coffers have swollen over the years as a result of both federal and local decisions. In this fattened environment, there are countless opportunities to improve how government works and spends other people's money. To that end, it would be prudent for the Legislature to require cities and counties to undergo a third-party efficiency audit before being allowed to petition voters for a large tax increase at an election seeking to exceed the voter-approval tax rate.¹

Key Points

- Historically, governments have struggled to evaluate their own spending objectively. As a result, government budgets and programs have tended to grow larger than necessary.
- Efficiency audits—also known as performance audits—can help decision makers evaluate a governmental entity's budget and operations to ensure sound management and a prudent use of tax dollars.
- The Legislature should require cities and counties to undergo a third-party efficiency audit before holding an election to exceed the voter-approval tax rate.
- As envisioned, the governing body would not be required to adopt any of the audit's recommendations; however, it should be mandatory that any findings be disclosed to and discussed with the public.
- The deluge of one-time federal monies requires an extra measure of vigilance and taxpayer protection.

¹ Senate Bill 2 (86R; 2019) defines the voter-approval tax rate as: "the highest tax rate that (name of taxing unit) may adopt without holding an election to seek voter approval of the rate" (p. 67). For cities, counties, and certain special districts, the voter-approval tax rate may not be set at a threshold that increases the amount of property tax revenue collected year-over-year by more than 3.5% without voter approval.

What Are Efficiency Audits?

Efficiency audits are one of three types of audits performed on a regular basis.² The International Organisation of Supreme Auditing Institutions (INTOSAI) defines it as:

an independent, objective and reliable examination of whether the government undertakings, systems, operations, programmes, activities or organizations are operating in accordance with the principles of economy, efficiency and effectiveness, and whether there is room for improvements. Auditors here review any subject matter from the perspectives of economy, efficiency, and effectiveness. ([INTOSAI, 2018, p. 7](#))

In general, an efficiency audit will provide information and insight on aspects of the government organization under review, including a budget analysis, recommendations for improving efficiency, and a list of opportunities for further improvement. The ideal type is performed by a third party that does not have any long-term interest in the entity audited. Its chief advantage is that it offers “a comprehensive examination of a governmental entity’s budget and operations. It is conducted for the purpose of identifying opportunities to reduce expenditures and better use resources” ([Texas Public Policy Foundation \[TPPF\], 2020, para. 3](#)).

An efficiency audit may assume many different forms; however, these types of in-depth studies will generally investigate elements of a similar sort, including:

- Efficiency gains and cost reductions that can be realized through administrative discretion, legislative changes, or by the enactment of ordinance or charter amendment;
- Opportunities to streamline programs, departments, and positions;
- Best practices that allow federal, state, or local governments to better share resources, such as personnel and equipment, and that improve personnel accountability in areas such as overtime;
- The nature and structure of federal funds received, including matching requirements and maintenance of effort requirements. Identify possible redundancies and overlap;

- Processes that can be made more cost-effective through the introduction of competitive bidding practices; and
- Programs, departments, and functions that merit further study. ([TPPF, 2019, para. 8](#))

Government Auditing Standards

Any efficiency audit on a county or city government should be conducted according to the generally accepted government auditing standards, as provided in the *Yellow Book* ([U.S. Government Accountability Office \[GAO\], n.d.](#)). The GAO develops best practice guidelines and requirements for auditors of federal, state, and local governments. GAO regularly updates and publishes its government auditing standards in the *Yellow Book*, which include “requirements for audit reports, professional qualifications for auditors, and audit organization quality control” ([“About The Yellow Book” section](#)). According to the organization:

Performance audits provide objective analysis, findings, and conclusions to assist management and those charged with governance and oversight with, among other things, improving program performance and operations, reducing costs, facilitating decision making by parties responsible for overseeing or initiating corrective action, and contributing to public accountability. ([GAO, 2021, pp. 10–11](#))

In addition to GAO’s standards, auditors may also be guided by INTOSAI, which is an international association of auditors that works with other auditing institutions to establish standards for auditing and governance in the public sector ([INTOSAI, n.d., “About us” section](#)). Similar to the efficiency audit requirements recently established by the Legislative Budget Board for independent school districts ([HB 3, 2019, pp. 1–3](#)), INTOSAI’s public-sector auditing standards seek to ensure that “governments and other public-sector entities exercise responsibility for the use of resources derived from taxation and other sources in the delivery of services to citizen and other recipients” ([INTOSAI, 2019, p. 10](#)).

Efficiency Audit Examples

Washington State: Initiative 900

In November 2005, voters in Washington state approved a ballot measure called Initiative 900 ([2005](#)), which provides the state auditor with authority to conduct performance

² The other two types of audits performed regularly are financial audits and compliance audits.

audits on nearly all government types and activities. It was passed along the following lines:

It is absurd for politicians to unilaterally impose tax increases or to seek voter approval for tax increases without first learning if we're getting the biggest bang for the buck from [Washington state's] current tax revenues. This measure requires the state auditor to conduct independent, comprehensive performance audits on state and local governments, agencies, programs, and accounts. ... The performance audits required by this common sense initiative will identify solutions to our public policy problems, saving the taxpayers billions of dollars. ([Initiative 900, 2005, p. 2](#))

Initiative 900 ([2005](#)) requires the performance audits to be conducted according to the government auditing standards of the GAO. Initiative 900 also authorizes the state auditor to contract with an independent third party to conduct the audit, requires an auditor to submit to the Legislature a report of each audit, and requires the Legislature to hold a public hearing to discuss and solicit public feedback regarding the audit ([p. 3](#)). To fund these in-depth investigations, the act “dedicate[d] a portion of the state’s existing sales and use tax (1/110th of 1%)” ([p. 2](#)).

Government Efficiency in Wyoming

In 2017, the 64th Wyoming Legislature enacted a bill ([SF 156, 2017](#)), which created “The Wyoming spending and government efficiency commission.” Among its many responsibilities, some of the commission’s oversight activities included:

- Review the current configuration of Wyoming state government and the duties and responsibilities of state agencies including identifying any potential areas of overlap and any programs that have accomplished their original objective or have otherwise become obsolete;
- Identify current opportunities for increasing efficiency and reducing costs through executive action or legislation;
- Identify areas for further study, including a recommendation of specific areas with a high likelihood for potential savings;
- Consider development and implementation of a program to incentivize the identification of potential efficiencies by state employees; ...

- Examine the opportunities for savings in the Medicaid programs subject to the following:
 - The examination shall determine the error rates in Medicaid enrollment through the Medicaid eligibility system, error rates in continuing enrollment in Medicaid and the costs of these error rates;
 - The commission is authorized to cause an audit of a sample of Medicaid enrollees to determine the error rates in enrollment and continued enrollment and the potential savings from correcting the error rates. The audit may be done by state personnel or through a contract with a private firm, or both;
 - The examination shall include a review of the Medicaid system to detect and correct errors in billing for Medicaid services; and
 - The examination shall include an inquiry concerning how the Medicaid program could reduce expenditures by reducing unneeded utilization of Medicaid services. ([pp. 2–3](#))

Furthermore, SF 156 “sunsetting” the commission, meaning it would expire at the end of 2017 if not reauthorized by the state Legislature ([p. 4](#)). In 2018, the 64th Wyoming Legislature extended the commission’s work with a new expiration date of June 30, 2020 ([SF 120, 2018, p. 9](#)). The state Legislature also created a “state savings and efficiency initiatives account” ([pp. 2, 9](#)) with an initial appropriation of \$10 million to fund the commission’s operations. Whereas the model efficiency audit should employ an independent external auditor to conduct the audit, the expenditures from Wyoming’s state savings and efficiency initiatives account required approval from the governor ([p. 2](#)). Ideally, a comprehensive investigation of executive agencies should be conducted absent the influence of the state’s top executive, to the greatest degree possible.

Efficiency Audits in Texas

The Texas Legislature has implemented multiple efficiency audits during recent legislative sessions, including some related to school districts ([Texas Education Code, Section 11.184](#)), the Department of Family and Protective Services (DFPS; [Texas Human Resources Code, Section 40.045](#)), and the Temporary Assistance for Needy Families (TANF) program ([Texas Government Code, Section 531.005522](#)). The most robust of these audit requirements is the one targeted at school district excess.

The 86th Texas Legislature enacted comprehensive school finance reforms, which included a requirement that school districts undergo an efficiency audit under certain circumstances ([HB 3, 2019, pp. 1–3](#)). That is, if a school district wishes to adopt a maintenance and operations (M&O) tax rate that produces property tax revenue in excess of a certain amount, then it must first conduct an audit before holding a voter-approval tax rate election. Using an internal auditor, a school district must undergo an efficiency audit that investigates its fiscal management, efficiency, and utilization of resources, as established by Legislative Budget Board guidelines ([Texas Education Code, Section 11.184](#)). Any audit findings must be disclosed to the public, and local elected officials are required to hold public hearings discussing the audit's recommendations. Since the enactment of HB 3, multiple school districts ([Arlington ISD, 2020](#); [Eanes ISD, 2020](#); [Mansfield ISD, 2021](#)) have implemented an efficiency audit to increase the district's M&O tax rate.

Building on this success, the 87th Texas Legislature passed House Bill 1516 ([2021](#)) and House Bill 2374 ([2021](#)), which require periodical efficiency audits for TANF funding and DFPS, respectively. According to the General Appropriations Act for the 2022–2023 biennium ([SB 1, 2021](#)), Texas will spend approximately \$4.6 billion on child and family welfare services through DPFS ([p. II-1–II-2](#)), which includes more than \$93 million for TANF grants ([p. II-37](#)).

Expanding Efficiency Audits to Other Local Government Types

Circumstances today make it an opportune time to encourage effective and efficient fiscal practices at the local level. Cities and counties in particular have received an infusion of federal aid while simultaneously reaping excessive property tax revenues over the years. These two factors present a real challenge to taxpayers and proponents of the Texas Model.

Influx of Federal Aid

In 2020, Congress passed the Coronavirus Aid, Relief, and Economic Security (CARES) Act ([2020](#)). The CARES Act established the “Coronavirus Relief Fund” (CRF; [p. 501](#)), which provided \$150 billion to state, local, and tribal governments to mitigate the impact of the COVID-19 pandemic. Texas governments received more than \$11.2 billion in total from this fund ([Driessen, 2021, p. 4](#)). The U.S. Treasury distributed \$3.2 billion in direct CRF payments to Texas' largest cities and counties, whereas the state received

the remaining \$8 billion in CRF funds for the state's less populated local governments ([U.S. Department of the Treasury, n.d.-a, p. 7](#)). The U.S. Treasury may recoup—or recover—CRF dollars from a state or local government that improperly uses the federal funds ([CARES Act, 2020, p. 224](#)). This provides an incentive to spend this money prudently, and implementing efficiency audits for local governments is one way to help achieve this financial prudence.

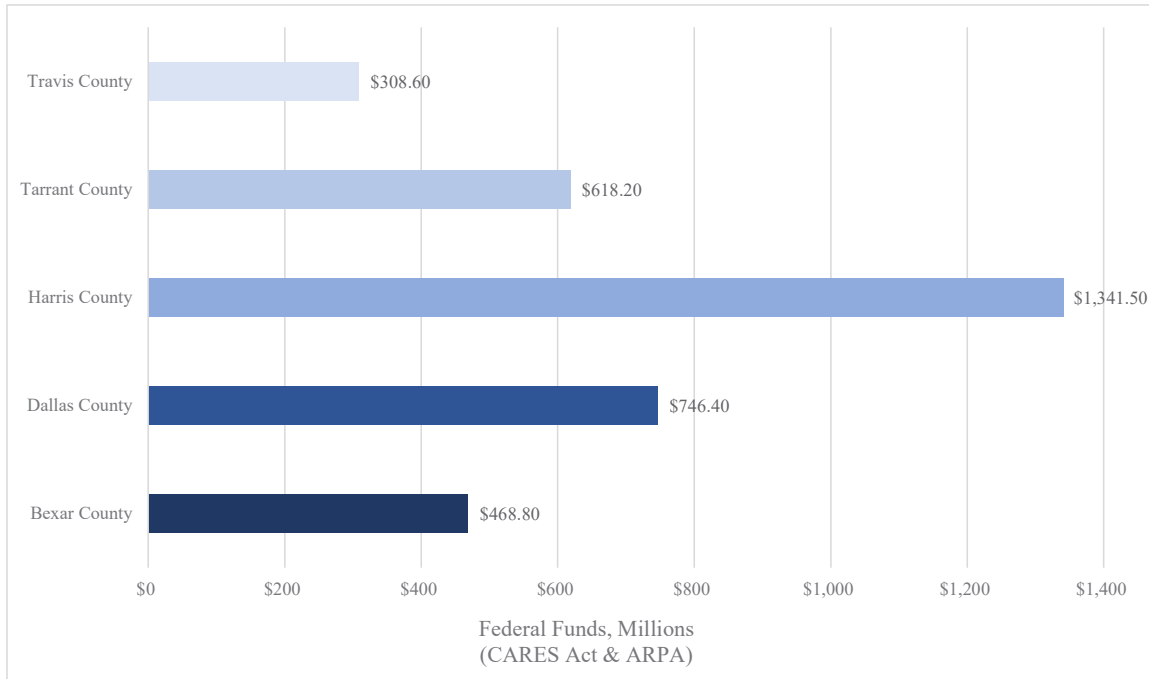
Congress provided state and local governments with additional federal funding with the passage of the American Rescue Plan Act ([ARPA, 2021](#)). ARPA created the Coronavirus State and Local Fiscal Recovery Funds (SLFRF) program, which appropriated an additional \$350 billion to state and local governments ([U.S. Department of the Treasury, n.d.-b](#)). The SLFRF program includes nearly \$230 billion ([ARPA, 2021, p. 223](#)) for state governments and \$130 billion for local governments ([p. 228](#)). Texas local governments will receive approximately \$10.5 billion from the SLFRF program, including \$1.4 billion for smaller cities and counties, \$3.4 billion for major cities, and \$5.7 billion for major counties ([Texas Comptroller of Public Accounts, n.d.-a, p. 1](#)). This additional infusion of federal funding undergirds the urgent need for efficiency audits among Texas local governments.

Figure 1 shows the federal funds received by Texas' largest counties from the CARES Act and ARPA, whereas **Figure 2** provides these figures for the state's largest municipalities.

Soaring Property Tax Revenues

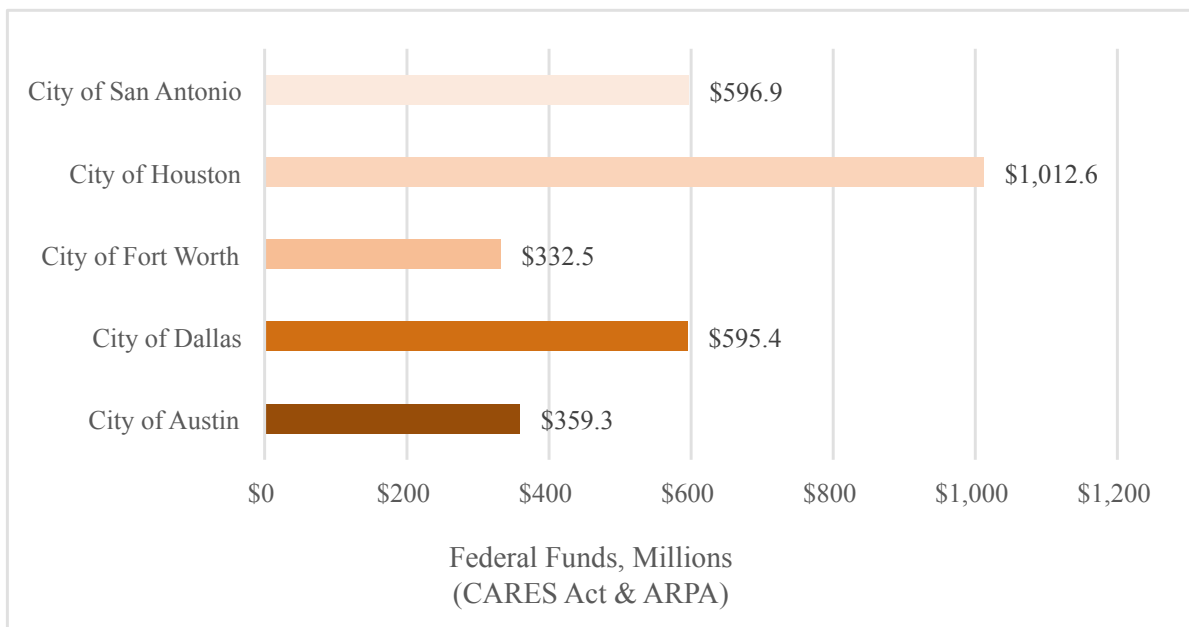
The amount of property tax revenues generated by Texas' local taxing jurisdictions has continued to grow much faster than the growth in each local government's population plus inflation. From 1998 to 2019, the total property tax levy among all of Texas' local taxing jurisdictions (cities, counties, school districts, and special purpose districts) consistently increased ([Texas Comptroller of Public Accounts, 2020, p. 7](#)). As shown in **Figure 3**, school districts have led the growth in property tax levies from 1998 to 2019. To help mitigate the fast-growing nature of this burden, the Texas Legislature enacted comprehensive reforms to the state's school finance system with the passage of House Bill 3 ([2019](#)). Among many provisions, the enacted legislation requires that a school district conduct an efficiency audit before it is allowed to hold a voter-approval tax rate election ([pp. 1–3](#)). For school districts, the voter-approval tax rate is defined as “The highest tax rate the district can adopt before requiring

Figure 1
Federal Funds to Counties (in Millions of Dollars)



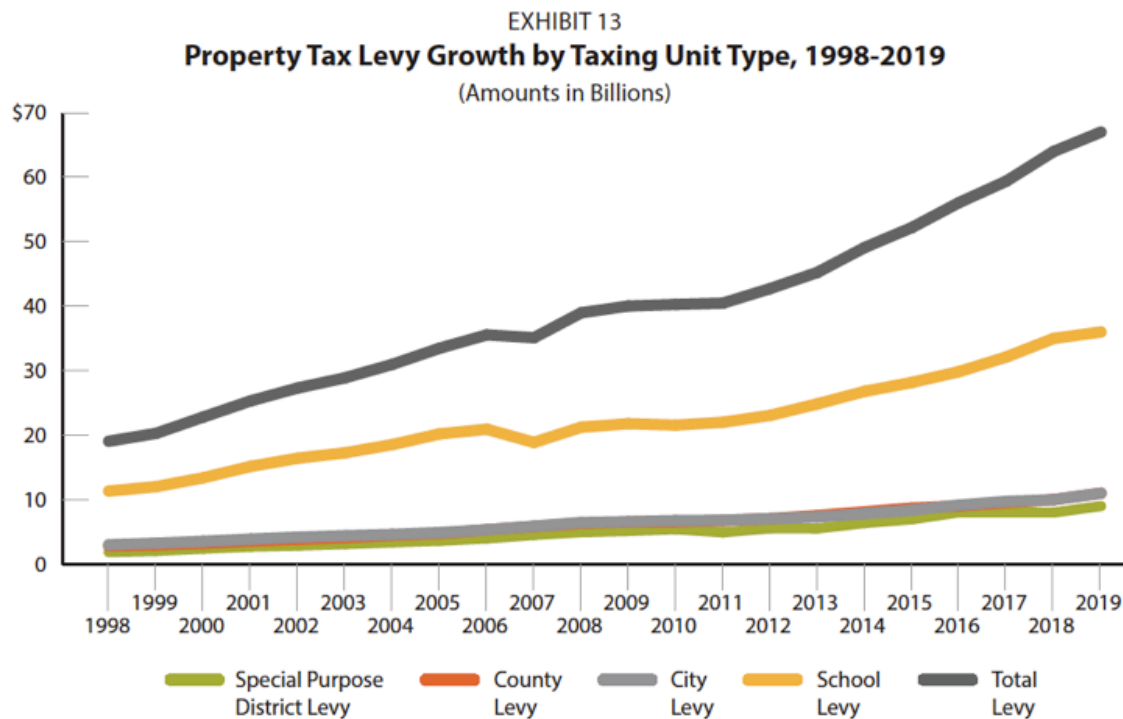
Note. Data from *Allocation for Counties*, U.S. Department of the Treasury, n.d.-d (https://home.treasury.gov/system/files/136/fiscal-recoveryfunds_countyfunding_2021.05.10-1a-508A.pdf) and *Coronavirus State and Local Fiscal Recovery Funds*, U.S. Department of Treasury, n.d.-b (<https://home.treasury.gov/system/files/136/Payments-to-States-and-Units-of-Local-Government.pdf>).

Figure 2
Federal Funds to Cities (in Millions of Dollars)



Note. Data from *Allocations to Metropolitan Cities*, U.S. Department of the Treasury, n.d.-c (<https://home.treasury.gov/system/files/136/Allocation-Methodology-for-MetropolitanCities-508A.pdf>) and *Payments to States and Eligible Units of Local Government*, U.S. Department of the Treasury n.d.-b (<https://home.treasury.gov/system/files/136/Payments-to-States-and-Units-of-Local-Government.pdf>).

Figure 3
 Property Tax Levies Among All Texas Local Governments



Note. Graph reproduced from *Biennial Property Tax Report*, Texas Comptroller of Public Accounts, 2020, p. 7 (<https://comptroller.texas.gov/taxes/property-tax/docs/96-1728.pdf>).

voter approval at an election” ([Texas Education Code, Section 44.004\(c\)\(8\)](#)). School district efficiency audits are discussed earlier in this paper.

Figure 4 displays the average population growth and property tax levy growth among Texas’ most populated cities (Austin, Dallas, Fort Worth, Houston, and San Antonio) and counties (Bexar, Dallas, Harris, Tarrant, and Travis counties). From fiscal years 2017 to 2021, the state’s largest cities experienced an average population increase of 3.03%. Yet, the total amount of property taxes levied by these cities increased by 14.82%. During a period of only five years, the burden of municipal tax rates has grown nearly 12 percentage points faster than taxpayers’ ability to pay the tax.

From fiscal years 2017 to 2021, the state’s largest counties experienced an average population increase of 3.38%. Yet, the total amount of property taxes levied by these cities increased by 7.15%. Like the municipal property tax, the burden of county tax rates has continued to increase faster than taxpayers’ ability to pay the tax—by almost 4%.

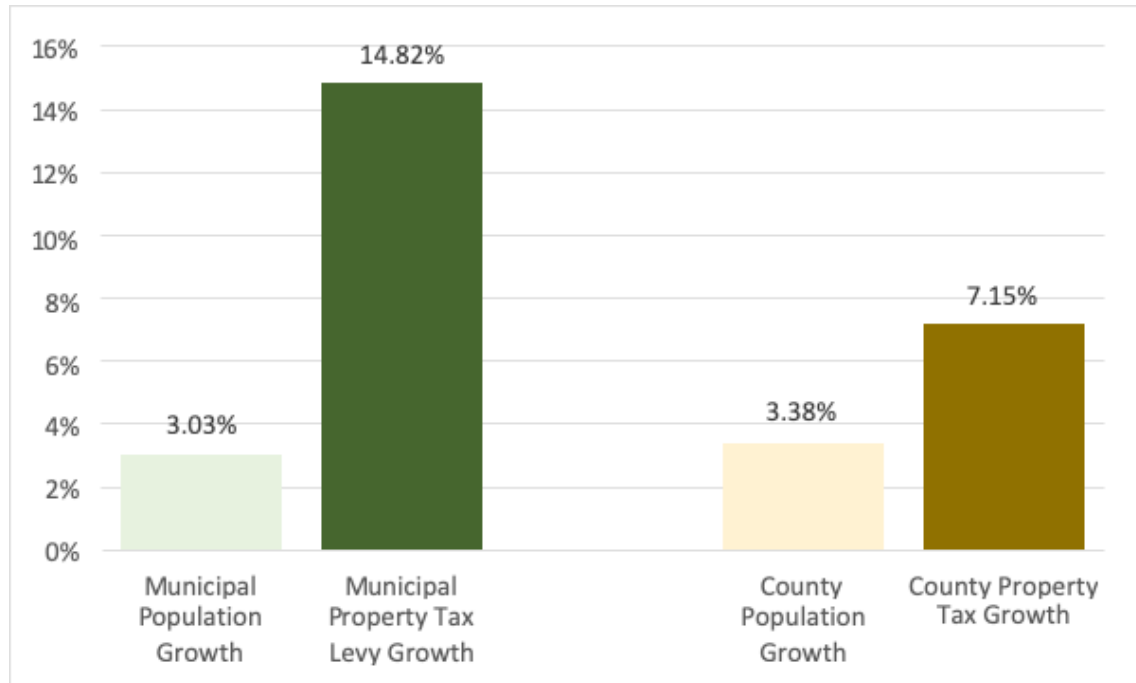
Elements to Incorporate in Any Efficiency Audit Requirement

If state lawmakers consider developing a policy prescription to require cities and counties to undergo an efficiency audit under certain circumstances, then there are several elements that they should incorporate into any final product. These may include ensuring auditor independence, guaranteeing access to information, disclosing any findings publicly, and discussing any recommendations publicly.

Independence

The guidelines requiring these efficiency audits should ensure that auditors remain independent from the program or entity being audited, including independence regarding the oversight of audits and approval for conducting audits. Providing organizational independence between the auditors and the program or entity being audited ensures that a managing authority does not “interfere with investigations [or] prevent full disclosure of issues” ([Association of Local Government Auditors \[ALGA\], 2006, p. 4](#)). The use of an independent auditor or independent audit committee may also “enhance accountability[,] earn and increase taxpayer confidence and respect for government[,] and] provide an

Figure 4
Fiscal Trends Among Large Local Governments, Fiscal Year 2017–21



Note. Data from *Tax Rates and Levies*, Texas Comptroller of Public Accounts, n.d. (<https://comptroller.texas.gov/taxes/property-tax/rates/>). The total amount of property taxes levied among local governments includes the maintenance and operation (M&O) and interest and sinking (I&S) tax rates. The data is adjusted for inflation by using real 2022 dollars as of February 2022.

independent and objective perspective” (ALGA, 2007, p. 10). Although many Texas counties and cities employ an internal auditor, the best way to conduct an efficiency audit is by contracting with a third party whose employees are not subject to administrative oversight from the affected entity. By contracting with a third party, cities and counties can further ensure that the auditing entity is qualified, experienced, and has a track-record of success.

Access to Information

According to the Association of Local Government Auditors (ALGA, 2014), the fundamental elements of an effective audit must ensure auditors have unrestricted access to the program or entity’s employees and records (p. 2). For example, an external auditor of a city or county must have the proper resources to conduct a thorough efficiency audit, including competent leadership and staff. If an auditor has the necessary resources to conduct an audit but does not have open access to important documents—like personnel records and financial statements—the auditor will be unable to conduct a proper efficiency audit.

Disclosure

An audit should include other critical aspects such as public reporting and responding to an audit’s findings (ALGA, 2014, p. 2). An external auditor must report any of their audit findings to a committee or entity independent of the audited entity or program. According to ALGA, independent audit committees lead to greater government accountability and protect auditors from any conflict of interest (ALGA, n.d., p. 1). Any findings ought to be made publicly available, and interested parties should have ample opportunity to digest the content before any official action is taken or discussed.

Public Discussion

Once an audit has been performed and the information publicly disclosed, the ideal reform will require the affected governmental entity to hold one or more public meetings to discuss the findings. The purpose of the meeting(s) is to allow the public to engage with their local elected officials on how the governmental entity might improve its budget or operations. While the governmental entity should not be required to adopt any of the recommendations put forward

in an audit, elements such as this, which encourage transparency and public participation, should be built into any legislative proposal.

Recommendation

Efficiency audits would provide an invaluable tool for boosting confidence in city and county operations as well as ensuring sound performance. What's more, this mechanism could be added to existing taxpayer protections in such a way that is not intrusive.

Consider that the Texas Legislature passed Senate Bill 2 (2019) in response to the rising property taxes levied by cities and counties. SB 2 requires that most cities and counties receive voter-approval before adopting a maintenance and operations tax rate that increases the tax levy by more than 3.5%. This type of election is called a voter-approval tax

rate election (VATRE). In 2023, state lawmakers could add a requirement onto VATREs that compels a governmental entity to undergo a third-party audit before being allowed to hold a tax increase election. Such a requirement was contemplated in 2021.

Senate Bill 1437 (2021), which did not pass and make it into law, would have required cities or counties to conduct an efficiency audit before seeking voter approval to increase the voter-approval tax rate of the city or county, in much the same way that is already required of school districts. A reform like SB 1437 “would bring an extra measure of transparency, accountability, and assurance to taxpayers” (Quintero, 2021, p. 1). Given the dramatic rise in local debt, property taxes, and the receipt of federal funds relating to COVID-19, this is the sort of taxpayer protection that is very much needed now. ★

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ABOUT THE AUTHORS



James Quintero is the policy director for the Texas Public Policy Foundation's Government for the People initiative. Having joined the Foundation in 2008, Quintero's research covers a wide range of issues, mostly related to local government matters, including: taxes, spending, debt, transparency, annexation, and pension reform. His work has been featured in the *New York Times*, *Forbes*, *Fox News*, *Breitbart*, and more.

Quintero received an M.P.A. from Texas State University and a B.A. from the University of Texas at Austin. He is currently seeking a Ph.D. in public policy from Liberty University.

Quintero and his wife, Tricia, are blessed with five beautiful children, a Great Dane, a Boston Terrier, and an exceptionally large grocery bill.



Parker Stathatos was a legislative fellow at the Foundation. Stathatos was a legislative director for a state representative in Texas' 87th Legislature. He managed a diverse bill package and helped pass 12 bills into law, including policies related to human trafficking, critical infrastructure, blockchain technology, virtual currency, civics education, criminal justice reform, and family welfare.

Prior to his time at the Texas Capitol, Stathatos participated in the fall 2020 White House Internship Program in the Office of the Senior Advisor for Policy. He was also previously an intern at the Foundation.

Stathatos has a B.A. in government and history from the University of Texas at Austin. In his spare time, he enjoys traveling, exploring new places, and spending time with his family and friends.

About Texas Public Policy Foundation

The Texas Public Policy Foundation is a 501(c)3 non-profit, non-partisan research institute. The Foundation promotes and defends liberty, personal responsibility, and free enterprise in Texas and the nation by educating and affecting policymakers and the Texas public policy debate with academically sound research and outreach.

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